Analysis

Department of Revenue

Private Collection Firms Report

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Request: Acknowledge receipt of a report on Private Collection Firms.

Recommendation: Acknowledge receipt of the report.

Analysis: The budget report for SB 5538 (2013), the primary 2013-15 budget bill for the Department of Revenue (DOR), included the following budget note:[1]

> The Department of Revenue shall report to the Legislature in 2014 on the use of private collection firms (PCF) including: age of accounts sent to PCF, amount of accounts turned over to the PCF (total and individual), time it takes PCF's to collect past due accounts, collection rate, and the amount and type of fees charged to clients.

In requesting this information, the Legislature is essentially asking whether the agency has the correct mix of in-house vs. private collection firm activities.

The Legislative Fiscal Office (LFO), as part of its *Report on Liquidated and Delinquent Accounts Receivable for June 30th, 2013*, reported that DOR has $738.3 million in outstanding debt for 152,158 accounts.

DOR undertakes collection actions even when a debt is subsequently referred to a PCF. DOR, itself a public collections agency, undertakes initial efforts and, if the debt remains uncollected, continues its collection effort, but transfers the debt to one of two private collection firms (PCF). While a debt is assigned to a PCF, DOR may issue administratively a garnishment at the request of a PCF, intercept state tax refunds, and accept payments directly from taxpayers. If DOR collects revenue on a debt assigned to a PCF, the agency applies the payment to the taxpayer's debt and then notifies the PCF. Therefore, any DOR collection on a debt transferred to a PCF positively impacts the PCF's collection rate.

In general, DOR transfers debt to PCFs if there has been no payment on the account for one year as required by statute or earlier under the following circumstances: (a) taxpayer has been identified as being out-of-state; (b) a new debt is companionated or combined with an existing taxpayer's account previously transferred to a PCF; and (c) some small debt. A debt can be cycled through a PCF multiple times and through multiple PCFs.

DOR states that, administratively, it has some automated processes and procedures, but outside of that its ability to work with PCFs is highly manual, which constrains its use of PCFs. DOR states that investments in staff and past information technology automation projects have been limited,

[1] The DOR limited its response to personal income tax and business tax liabilities; The legal authority to send Other Agency Accounts program debt to private collections resides with the state agency responsible for the collection of the debt.

primarily because the return on investment is lower than other in-house collection initiatives. DOR's Collection Agency Program has a biennial budget of $1.2 million (10.00 FTE).

The following is data for fiscal year 2013. The agency reports that there are 39,100 accounts valued at $310.1 million that were assigned to PCFs. The average liability is $2,100. The value transferred includes principle, interest, penalties, and fees before any PCF added collections fees that the PCF's charge and retain. The average age of this debt was 2.7 years. It took on average approximately 227 days for the first payment to be made on the debt. The estimated PCF collection rate was 3.5%, which "…nearly 25 percent of [value] payments on liabilities after being assigned to a PCF were from garnishments. For the same period, 17.5 percent of payments came from automated tax refund offsets." The LFO *Report on Liquidated and Delinquent Accounts Receivable for June 30th, 2013* reported that state agencies overall PCF collection rate was 1.4%.

DOR has contracts with two of three statewide PCF vendors, each of which has a unique price agreement and fee structure based on the percentage of the amount collected. The amount collected differs from the amount of the debt sent to DOR as it includes added penalties, fees, and interest. Such collection fees vary from 26% to 10%, depending upon if DOR is the issuer of a garnishment. In addition, there are fees for the recording of liens, garnishments, late payments, and federal tax offset. For FY2013, the two private collection firms earned $513,000 and $348,000 in collection fees, respectively.

DOR believes that a comparison of collection results between DOR and PCFs is uninformative because the efforts undertaken by each organization differ. The report made no mention of its use of best practices.

The Legislature in 2013 approved funding of the replacement of the agency's aging legacy applications. While the Core System Replacement project (CSR) is expected to increase DOR's capability to send debt to PCFs, it will simultaneously reduce the agency's need to do so as a modernized application platform will allow for a more efficient and complete in-house processing of collections (e.g., more timely collections, skip tracing, scoring, data matching, prioritization, etc.)

From the DOR report it is difficult to ascertain whether the agency has the correct mix of in-house vs. PCF efforts. Hopefully, this will change once the CSR project has been fully implemented.

The Legislative Fiscal Office recommends acknowledging receipt of the report.